2004

Armand L. Smith Individually and as Trustee for the Armand L. Smith, Jr And Shannon S. Windham Trusts, and Virginia L. Smith, Individually v. Price Development comapny, nka Fairfax Realty Inc., North Plains Land Company, LTD, The state Treasurer, Edward T. Alter of the State of Utah, for and in behalf of The State of Utah : Reply Brief

Utah Supreme Court

Robert S. Campbell, Jr.; Jennifer J. Anderson Whitlock; Van Cott, Bagley, Cornwall & McCarthy; Attorneys for Appellees.
Reed L. Martineau; Snow, Christensen; Kevin V. Olson; Assistant Attorney General; Mark L. Shurtleff; Attorney General; James S. Jardine; Attorneys for Appellants/Defendants .

IN THE UTAH SUPREME COURT

ARMAND L. SMITH, Individually and as Trustee for the Armand L. Smith, Jr. And Shannon S. Windham Trusts, and VIRGINIA L. SMITH, Individually, Plaintiffs/Appellees, v. PRICE DEVELOPMENT COMPANY, a Utah Corporation, n/k/a FAIRFAX REALTY, INC., NORTH PLAINS LAND COMPANY, LTD., a Utah limited partnership, and NORTH PLAINS DEVELOPMENT COMPANY, LTD., a Utah limited partnership, Defendants, The State Treasurer, Edward T. Alter of the State of Utah, for and in behalf of THE STATE OF UTAH, Rule 19 Defendant/Appellant.	Case No. 20040675

REPLY BRIEF

Appeal from the Summary Judgment Order dated June 24, 2004 which was directed to be the final judgment against the State of Utah pursuant to Rule 54 by the Third District Court in and for Salt Lake County, State of Utah, the Honorable Frank G. Noel, District Court Judge, Presiding.

James S. Jardine
RAY, QUINNEY & NEBEKER
36 South State Street Suite 1400
Salt Lake City, Utah 84111
Attorneys for Defendants

Reed L. Martineau
SNOW, CHRISTENSEN
10 Exchange Place, 11th Floor
P.O. Box 45000
Salt Lake City, Utah 84145-5000
Attorneys for Defendants

Robert S. Campbell, Jr.
Jennifer J. Anderson Whitlock
VAN COTT, BAGLEY, CORNWALL
& McCARTHY, P.C.
50 South Main, Suite 1600
Salt Lake City, Utah 84144-0450
Attorneys for Plaintiffs/Appellees

Kevin V. Olsen
Assistant Attorney General
Mark L. Shurtleff
Attorney General
160 East 300 South, 5th Floor
P.O. Box 140853
Salt Lake City, Utah 84114-0853
Attorneys for Appellant

IN THE UTAH SUPREME COURT

ARMAND L. SMITH, Individually and as Trustee for the Armand L. Smith, Jr. And Shannon S. Windham Trusts, and VIRGINIA L. SMITH, Individually, Plaintiffs/Appellees, v. PRICE DEVELOPMENT COMPANY, a Utah Corporation, n/k/a FAIRFAX REALTY, INC., NORTH PLAINS LAND COMPANY, LTD., a Utah limited partnership, and NORTH PLAINS DEVELOPMENT COMPANY, LTD., a Utah limited partnership, Defendants, The State Treasurer, Edward T. Alter of the State of Utah, for and in behalf of THE STATE OF UTAH, Rule 19 Defendant/Appellant.	)	Case No. 20040675

REPLY BRIEF

Appeal from the Summary Judgment Order dated June 24, 2004 which was directed to be the final judgment against the State of Utah pursuant to Rule 54 by the Third District Court in and for Salt Lake County, State of Utah, the Honorable Frank G. Noel, District Court Judge, Presiding.

James S. Jardine
RAY, QUINNEY & NEBEKER
36 South State Street Suite 1400
Salt Lake City, Utah 84111
Attorneys for Defendants

Reed L. Martineau
SNOW, CHRISTENSEN
10 Exchange Place, 11th Floor
P.O. Box 45000
Salt Lake City, Utah 84145-5000
Attorneys for Defendants

Robert S. Campbell, Jr.
Jennifer J. Anderson Whitlock
VAN COTT, BAGLEY, CORNWALL & McCARTHY, P.C.
50 South Main, Suite 1600
Salt Lake City, Utah 84144-0450
Attorneys for Plaintiffs/Appellees

Kevin V. Olsen
Assistant Attorney General
Mark L. Shurtleff
Attorney General
160 East 300 South, 5th Floor
P.O. Box 140853
Salt Lake City, Utah 84114-0853
Attorneys for Appellant

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page

FEDERAL CASES

STATE CASES

STATE STATUTES

MISCELLANEOUS

IN THE UTAH SUPREME COURT

ARMAND L. SMITH, Individually and as Trustee for the Armand L. Smith, Jr. And Shannon S. Windham Trusts, and VIRGINIA L. SMITH, Individually, Plaintiffs/Appellees, v. PRICE DEVELOPMENT COMPANY, a Utah Corporation, n/k/a FAIRFAX REALTY, INC., NORTH PLAINS LAND COMPANY, LTD., a Utah limited partnership, and NORTH PLAINS DEVELOPMENT COMPANY, LTD., a Utah limited partnership, Defendants, The State Treasurer, Edward T. Alter of the State of Utah, for and in behalf of THE STATE OF UTAH, Rule 19 Defendant/Appellant.	)	Case No. 20040675

REPLY BRIEF

ARGUMENT

I. THE SMITHS FAILED TO MEET THEIR HEAVY BURDEN TO SHOW THAT UTAH CODE ANN.§78-18-1(3)(1989) IS UNCONSTITUTIONAL.

A. <u>There is a strong presumption that Utah Code Ann.§78-18-1(3)(1989) is constitutional.</u>

At the beginning of the their arguments, the Smiths quote the U.S. Supreme Court in City of Mobile v. Bolden, 446 U.S. 55, 76 (1980), as stating that "[i]t is of course true that a law that impinges upon a fundamental right explicitly or implicitly secured by the Constitution is presumptively unconstitutional." (Appellee's Brief at 12). This is not a correct statement of the law to be followed in this case.

In determining the constitutionality of statutes, it is well settled "that legislative enactments are endowed with a strong presumption of validity and will not be declared unconstitutional unless there is no reasonable basis upon which they can be construed as conforming to constitutional requirements." City of Monticello v. Christensen, 788 P.2d 513, 516 (Utah 1990).

The rules that surround this presumption of validity are explained in Baker v. Matheson, 607 P.2d 233, 236 (Utah 1979) (quoting State v. Packer Corporation, 77 Utah 500,508-509, 297 P. 1013,1016 (1931), affirmed, 285 U.S. 105, 52 S.Ct. 273, 76 L.Ed. 643). There, this Court stated that in regards to statutes that don't affect fundamental rights there is a heavy burden placed on the party who challenges the constitutionality of the statute to "clearly and manifestly" establish that the statute violates a provision of the constitution. Baker, 607 P.2d at 237 n.2. Every presumption must be indulged in favor of the constitutionality of the act, and every reasonable doubt resolved in favor of its validity. Id.,at 237 n.2. Further, this Court explained that it is the duty of the court to sustain the enactment if by any fair interpretation of the statute the legislation can be upheld. This is so even though judges may view the act as inopportune

or unwise. It is not within the province of the judiciary to question the wisdom or the motives of the Legislature in the enactment of the statute. Id., at 237 n.2.

The Baker court explained the reasons for these rules:

> These general principles, although applied with varying degrees of stringency depending upon the nature of the statutory provision to be construed, establish general guidelines for the functioning of a system of government based upon a separation of powers in which the popular will is effectuated by the legislative branch and the power of constitutional review of legislative enactments is vested in the judiciary. Due respect for the legislative prerogative in lawmaking requires that the judiciary not interfere with enactments of the Legislature where disagreement is founded only on policy considerations and the legislative scheme employs reasonable means to effectuate a legitimate objective. In matters not affecting fundamental rights, the prerogative of the legislative branch is broad and must by necessity be so if government is to be by the people through their elected representatives and not by judges.

Baker, 607 P.2d 233 at 236.

It is also well settled that where there are two possible interpretations of a statute, one that would make the statute unconstitutionally invalid and the other valid, the court should adopt a construction that will make the statute valid. Norman J. Singer, Statutes and Statutory Construction, §57:24 at 75 (6th ed. 2001). Apparently following this rule, this Court has stated that courts have a duty to construe a statute whenever possible to save it from unconstitutional infirmities, In Re Marriage of Gonzalez, 2000 UT 28, ¶ 23, 1 P.3d 1074, 1079, and that a court must not view pertinent parts of the statute in isolation for the purpose of finding fault with the statute and declaring it unconstitutional, Buhler v. Stone, 533 P.2d 292, 294 (Utah 1975).

In the present case, the Smiths assume that Utah Code Ann.§78-18-1(3)(1989) expressly takes away their vested right and make the legal conclusion that "[i]n the constitutional context, it is undeniable that the Smiths' property interests vested in the entire punitive damage judgment when it was entered on June 29, 2001." (Appellee's Brief at 13). The Smiths' legal conclusion can only be reached if this Court construes the statute without regard to well settled rules of statutory construction. (Appellant's Brief at 9). Since the statute does not expressly or implicitly take any vested right or other protected property interest away from the Smiths, it is not presumptively unconstitutional as the Smiths contend.

B. The Smiths are not able to clearly and manifestly establish that Utah Code Ann.§78-18-1(3)(1989) violates a protected right.

In the present case, because there is a strong presumption that Utah Code Ann.§78-18-1(3)(1989) is constitutional, the Smiths have the burden to clearly and manifestly show that the statute violates a constitutionally protected right. The Smiths have failed to meet this heavy burden in the following ways.

As noted above, the Smiths begin their argument with the legal conclusion that the entire judgment vested in them. They then state that "[t]he very integrity of final judgments in the State of Utah is in jeopardy in this appeal." (Appellee's Brief at 14). From there, the Smiths argue that under the vested rights doctrine, the legislature does not have the authority to take away rights that have been vested by judgment. (Appellee's Brief at 16).

The Smiths' reliance on the vested rights doctrine assumes that they are able to acquire a vested right in something that the legislature stated that they did not have a right to obtain. As previously argued by the State, the legislature has the power to modify the common law regarding punitive damages. (Appellant's Brief at 16). This includes limiting or abolishing such damages. The legislature enacted the Punitive Damage Awards Act in 1989, well before judgment was entered in this case. The judgment was therefore subject to the limitations imposed by that enactment. The trial court cannot grant to the Smiths by entry of a judgment more than what the law affords. Spanish Fork Westfield Irr.Co. v. District Court of Salt Lake County, 99 Utah 527, 104 P.2d 353, 359 (1940) (the court stated that a court of equity cannot create rights, but is limited to determine what rights the parties have and whether or in what manner it is just and proper to enforce them; and that these courts and courts of law are bound by positive provisions of statutes and cannot disregard constitutional and statutory requirements). Yet, that is at the foundation of each of the Smiths' arguments.

In addressing the plain language of the statute, the Smiths argue that the statute plainly "contemplates an entitlement to a punitive damage award, not judgment, but only if the punitive award is ever paid." (Appellees' Brief at 18). This construction of the statute makes no sense, especially when the words of the statute plainly state "in any judgment." The Smiths also ignore other plain language of the statute which simply requires the payor of any punitive damages judgment to remit a portion of the punitive damages to the state treasurer. Further, the Smiths' construction ignores legislative

intent. The legislature clearly did not intend to take any vested right away from the Smiths or any other such plaintiffs. On the contrary, it is clear that the legislature intended to limit the amount of punitive damages that plaintiffs such as the Smiths could expect to recover.

After addressing their plain language arguments, the Smiths then claim that "troubling questions plague the Treasurer's arguments" (Appellee's Brief at 18). They ask, "To begin with, when does the Treasurer claim that its 50% interest 'vested'? Also, vested in what?" They answer their own questions by stating that the State cannot have a vested interest in the judgment if it is qualified by the "condition or hypothesis"of being paid. (Appellee's Brief at 18, 19). They then ask other hypothetical questions assuming that the rights of the State cannot be determined. (Appellee's Brief at 19, 20).

These questions are troublesome for the Smiths because of the way that they want this Court to construe the statute. If the statute is construed as the State urges and the Smiths are only entitled to recover a portion of the punitive damages judgment, then the State's interest is created at the time that the judgment is entered and payment of the State's portion of the punitive damage award is to be remitted to the state treasurer by the judgment payor. Consequently, there is no "condition or hypothesis" to be met before the State's interest is created.

In addition, given the fact that the State has an interest in the punitive damages judgment at the time it was entered, there is no basis to reach the Smiths' implicit legal conclusion that the State could not enforce payment of its share of the

punitive damages as could any judgment creditor, whether through the Bankruptcy Court procedures or otherwise. Further, there is no basis to reach the Smiths' implicit legal conclusion that a settlement of the parties would negate the State's right to payment of its share of the punitive damages judgment. The hypothetical questions posed by the Smiths await resolution in an actual case that presents these issues. This case does not.

The fact that the Smiths defended on appeal the entire punitive damages judgment is no different than the fact that they initiated and litigated the lawsuit that resulted in the judgment. Once the appeal was concluded and the case remanded to the trial court, the final judgment entitled the State to a portion of the punitive damages that were awarded.

Although the language of the statute is simple and the legislative intent is clear, the trial court agreed with the Smiths that the State's interest triggers only if and when the judgment is paid; therefore, it ruled that an unconstitutional taking results. Thus, the statute is susceptible of two constructions, one that is within the legislature's authority and the other without. That being the case, this Court must adopt the construction that saves the statute from constitutional infirmity. To conclude otherwise, as the trial court did and as the Smiths urge this Court to do, is to attack our system of government where government is suppose to be by the people though their elected representatives and not by judges.

II. THE COLORADO CASE, KIRK v. DENVER PUBLISHING CO., 818 P.2d 262 (COLO. 1991) IS DISTINGUISHABLE FROM THIS CASE AND DOES NOT FOLLOW UTAH LAW.

The Smiths argue that there is case precedent for finding Utah Code Ann.§78-18-1(3)(1989) unconstitutional as a "taking" of their vested rights in the punitive damage judgment. (Appellee's Brief at 21). In making this argument, the Smiths rely upon Kirk v. Denver Publishing Co., 818 P.2d 262 (Colo.1991). Their reliance upon Kirk is misplaced. Contrary to the Smiths' assertions, the Colorado split-recovery statute is not "strikingly comparable" to Utah's split-recovery statute and the analysis of the Kirk court goes against Utah law.

A. The Colorado split-recovery statute is distinguishable in that it expressly disavows the state's interest until after the judgment is entered and collected.

The Colorado split-recovery statute is distinguishable from Utah's Punitive Damages Awards Act in two important ways. First, the Colorado statute expressly states that "[n]othing in [the statute] shall be construed to give the general fund any interest in the claim for exemplary damages or in the litigation itself at any time prior to payment becoming due."[1] Kirk, 818 P.2d at 266. Unlike the Colorado statute, Utah's split-

---

[1]Contrary to the Smiths' assertion that this phrase was mentioned by the court in passing as an "add-on" type of statement, the Kirk court found that "by its plain terms, [the Colorado statute] contemplates the entry, and the actual collection, of a final judgment on behalf of the injured party, for it is only after the time, effort, and expense of obtaining and actually collecting the judgment that the statutory grant of one-third interest comes into play." Kirk, 818 P.2d at 266. In addition, the court found the language to be an "implicit acknowledgment of the property interest created in the judgment creditor by virtue of the judgment itself." Kirk, 818 P.2d at 267.

recovery statute does not expressly disavow the State's interest until after the judgment is entered.

Second, the Colorado statute provided that one-third of all exemplary damages "collected" pursuant to the statute shall be paid into the state's general fund. When read together with the disavowal language, the word "collected" can only be read to mean that the state's interest in a portion of the punitive damage judgment would arise once the judgment was collected by the judgment creditor.

This is different from how the word "paid" is used in Utah's statute. Utah's statute states that in any judgment where punitive damages are awarded and paid, a portion of the punitive damages is to be remitted to the state treasurer. In Utah's statute, it is more reasonable to imply that the payor of the judgment has the duty to send the State's portion of the punitive damages judgment to the state treasurer than to imply that the duty rests with the judgment creditor after the judgment is collected. If the judgment creditor is wrongfully paid the State's portion, only then is the judgment creditor required to make a payment to the State. Therefore, the word "paid" in the Utah statute is not equivalent to the word "collected" in the Colorado statute as the Smiths contend.

B. The analysis of the Kirk court goes against Utah law.

The Kirk court concluded that the Colorado split-recovery statute effectuates a forced taking of the judgment creditor's property interest in the judgment and that it does so in a manner and to a degree unrelated to any constitutionally permissible governmental interest served by the taking. Therefore, it concluded that the

statute violated the constitutional prohibitions of taking private property without just compensation. The court explained that its conclusions were derived from "the nature of an exemplary damages award as a private property right, the confiscatory character of the 'taking' mandated by the statute, and the manifest absence of a reasonable nexus between the statutory taking of one-third of the exemplary damages award and the cost of any governmental services that arguably might support a significantly smaller forced contribution." Kirk, 818 P.2d at 265.

In its analysis of the nature of exemplary damages, the Kirk court explained that tort law generally provides for two types of monetary remedies for a civil wrong, i.e. compensatory damages to make the injured party whole and exemplary damages to punish and deter similar conduct in the future. The court found that because compensatory awards serve the reparative function of making the injured party whole as well as the secondary function of discouraging a repeat of the wrong and as a warning to others, exemplary damages serve in a somewhat similar fashion. Id. at 266. Although meant to punish and deter, the court concluded that exemplary damages also serve to compensate the plaintiff. Therefore, Colorado's split-recovery statute was viewed as a "forced contribution" from the plaintiff. Id. at 270. The court stated the following:

> As we previously observed, while a judgment for exemplary damages is designed to punish the wrongdoer and deter similar conduct by others, it is only available when a civil wrong has been committed under extremely aggravating circumstances and when the injured party has a successful claim for actual damages against the wrongdoer. In that sense, an exemplary damages award is not totally devoid of any and all reparative elements. More importantly, the forced contribution of one-third of the exemplary damages judgment is imposed not on the

> defendant wrongdoer who caused the injuries but upon the plaintiff who suffered the wrong.

Id. (emphasis added; citation omitted).

The Kirk court also reasoned that "the statutory disavowal in section 13-21-102(4) of any state interest in a claim for exemplary damages 'at any time prior to payment becoming due' is an implicit legislative acknowledgment of the property interest created in the judgment creditor by virtue of the judgment itself." Kirk, 818 P.2d at 267. Implicit in the court's conclusion is that regardless of the legislature's grant of one-third interest in the punitive damage judgment to the state, the judgment creditor has a protected property interest in the entire judgment.

The Kirk court's legal analysis goes against Utah law. First, exemplary or punitive damages do not serve a reparative function in the awarding of damages. Utah law clearly holds that even though they generally bear some reasonable relation to the amount of actual damages awarded, punitive damages are by nature not to compensate but to punish and deter future egregious conduct. Campbell v. State Farm Mut. Auto. Ins. Co., 2001 UT 89, ¶ 115, 65 P.3d 1134, 1167, rev'd on other grounds, 123 S.Ct. 1513,___U.S.___ (2003); Terry v. Zions Co-op Mercantile Institution, 605 P.2d 314, 328 (Utah 1979), overruled on other grounds, McFarland v. Skaggs Companies, Inc., 678 P.2d 298 (Utah 1984). Second, Utah law clearly does not recognize a right to a cause of action for punitive damages. Debry v. Cascade Enterprises, 879 P.2d 1353, 1359 (Utah 1994). Third, Utah law clearly recognizes the right of the legislature to modify the common law, including the awarding of punitive damages. Jackson v. Mateus, 2003 UT

18, ¶ 21, 70 P.3d 78, 83. Finally, the Kirk court's opinion runs contrary to the notion that a judgment creditor cannot obtain a vested interest in more than the law allows. See Spanish Fork Westfield Irr.Co. v. District Court of Salt Lake County, 99 Utah 527, 104 P.2d 353, 359 (1940).

C. Other state supreme courts have criticized the analysis that was made by the Kirk court.

It is notable that those state supreme courts that have had occasion to decide the constitutionality of their state's split-recovery statutes after Kirk have consistently echoed these same criticisms. For example, the Supreme Court of Missouri in Fust v. Attorney General for the State of Missouri, 947 S.W.2d 424 (Mo. 1997), upheld Missouri's split-recovery statute that allocated 50% of any punitive damage judgment to the state. In reaching this conclusion, the court distinguished the Missouri statute from the Colorado statute addressed in Kirk. Moreover, the court stated that "this Court does not agree with the implicit conclusion in Kirk that a plaintiff has a greater property interest in a judgment upon a tort claim than the interest recognized by law when the claim accrued." Id. at 431.

The Supreme Court of Alaska, in Anderson v. State of Alaska ex rel. Central Bering Sea Fishermen's Association, 78 P.3d 710 (Alaska 2002), affirmed the trial court's ruling that Alaska's split-recovery statute allocating one half of punitive damages to the state was constitutional. Writing for the court, Justice Bryner stated that he believed that "Kirk is implicitly based on a rationale inconsistent with that which is expressed in this opinion and thus disagree with it." Justice Bryner explained the reason

for his disagreement with Kirk by quoting from Fust v. Attorney General for the State of Missouri, 947 S.W.2d 424 (Mo. 1997). Anderson, 78 P.3d at 716 n. 30.

The Supreme Court of Oregon, in DeMendoza v. Huffman, 334 Or. 425, 452, 51 P.3d 1232, 1247 (2002), similarly questioned the soundness of the conclusions reached in the Kirk case and held that Oregon's split-recovery statute allocating 60 percent of each punitive damage award to the state's Criminal Injuries Compensation Account did not violate the Oregon Constitution. As the basis for its criticism, the court also quoted from Fust v. Attorney General for the State of Missouri, 947 S.W.2d 424 (Mo. 1997) . DeMendoza, 334 Or. at 452, 51 P.3d at 1247 n. 17.

Finally, in Chetham v. Pohle, 789 N.E.2d 467 (Ind. 2003), the Supreme Court of Indiana affirmed the trial court's ruling that there was no vested property right in the award of punitive damages, and that, as a result, Indiana's split-recovery statute requiring 75% of punitive damages to be deposited into violent crimes victims compensation fund did not violate the Takings Clauses of the state and federal constitutions. After making reference to the Kirk case, the court stated that it did not agree with the rationale in Kirk. Id. at 475.

As pointed out by the courts in Anderson v. State of Alaska ex rel. Central Bering Sea Fishermen's Association, 78 P.3d 710, 716 (Alaska 2002) and DeMendoza v. Huffman, 334 Or. 425, 452, 51 P.3d 1232, 1247 n.18 (2002), the Kirk court stands alone among the other state supreme courts in striking down a split-recovery statute as an unconstitutional taking. Each of the other state supreme courts has consistently held that

a plaintiff does not have a vested property right in punitive damages prior to the entry of a judgment and that the legislature has the authority to restrict or abolish punitive damage awards. Anderson v. State of Alaska ex rel. Central Bering Sea Fishermen's Association, 78 P.3d 710, 715 (Alaska 2002); Gordon v. State, 608 So.2d 800, 801 (Fla. 1992); Mack Trucks, Inc. v. Conkle, 263 Ga. 539, 541, 436 S.E.2d 635, 638 (1993); Shepherd Components, Inc. v. Brice Petrides-Donohue & Associates, 473 N.W.2d 612, 619 (Iowa 1991); Fust v. Attorney General for the State of Missouri, 947 S.W.2d 424, 431 (Mo. 1997); DeMendoza v. Huffman, 334 Or. 425, 444, 51 P.3d 1232, 1243 (2002); and Chetham v. Pohle, 789 N.E.2d 467, 471(Ind. 2003). The decisions in these cases follow Utah law. As a result, this Court should look to these cases for precedent and not the Kirk case.

D. The legislatures of Florida, Colorado and Kansas have asserted their authority to limit punitive damages by using statutory damage caps instead of split-recovery statutes in their efforts at tort reform.

There is one final point to make regarding the treatment of the other states' split-recovery statutes. The Smiths make an issue of the fact that the Florida, New York, and Colorado statutes were repealed, and that the Kansas statute has expired. The rest of the story is that the legislatures in Florida, Colorado and Kansas have each enacted statutes that put caps on the amount of punitive damages that a plaintiff may recover. FLA. STAT. §768.73 (with some exceptions, punitive damages may not exceed the greater of three times the actual damages or $500,000.00); COLO. REV. STAT. §13-21-102(1) (punitive damages in most cases are limited to amount of actual damages, though under

certain circumstances the court can increase the award to three times the actual damages); KAN. STAT. ANN. §60-3701 (with some exceptions, punitive damages may not exceed the lesser of the annual gross income of the wrongdoer or $5 million) Even though the use of split-recovery statutes has ended in these states as mentioned by the Smiths, these states' legislatures (including Colorado's) continue to address the need for tort reform by asserting their authority to limit the amount of punitive damages that are recoverable by plaintiffs. Similarly, the Utah Legislature has the authority to limit punitive damages. However, it has made the decision to do this by way of the split-recovery statute instead of statutory damages caps.

III. THE 2004 LEGISLATIVE AMENDMENTS TO THE PUNITIVE DAMAGES AWARDS ACT DO NOT SUBSTANTIVELY CHANGE THE PARTIES' RIGHTS.

The Smiths argue that "[i]n the 2004 session of the Utah Legislature, Section 78-18-1(3)(1989) was amended to introduce new substantive provisions that demonstrably changed the structure and vesting of the interest of the plaintiff obtaining a punitive damage judgment, as well as providing for a new interest of the State Treasurer in said judgment." (Appellee's Brief at 25). Contrary to this assertion, the 2004 Utah Legislature did not change the substantive rights of the parties by these amendments.

Although the original language of the statute directed the payor of the judgment to remit a portion of the punitive damages to the state, the amendments clarify that the judgment itself must include a provision that directs the judgment debtor to pay the State's portion of the punitive damages to the state treasurer. Although the State

always had the right to enforce its share of the punitive damages judgment similar to that of a judgment creditor, the amendments clarify that the State has the rights of a judgment creditor and stands on equal footing with the judgment creditor in securing a recovery, subject to the priority of payment of compensatory damages and attorney fees. In making these clarifications, the Legislature neither increased nor decreased the amount of punitive damages that a plaintiff is able to recover under the law. Therefore, the amendments did not substantively change the law regarding the rights of plaintiffs or the State.

IV. BECAUSE THE STATE HAS A PROPRIETARY INTEREST IN A PORTION OF THE PUNITIVE DAMAGE JUDGMENT, RECOVERY OF THAT PORTION OF THE JUDGMENT IS NOT INCOME TO THE SMITHS.

To support their argument that they may be liable for taxes on the entire punitive damages judgment which they insist vested in them, the Smiths point to Banaitis v. Commissioner of Internal Revenue, 340 F.3d 1074 (9th Cir. 2003), cert. granted, Comm'r v. Banks, 124 S. Ct. 1712, 2004 U.S. LEXIS 2384. (Appellee's Brief at 29). In that case, the taxpayer had obtained a jury judgment against Bank of California and Mitsubishi Bank for the following amounts: $196,389 for lost compensation, $500,000 for lost future compensation, $500,000 for emotional distress (Mitsubishi Bank), $125,000 for emotional distress (Bank of California), $3 million in punitive damages (Mitsubishi Bank) and $2 million punitive damages (Bank of California). The jury judgment was ultimately affirmed on appeal and the parties shortly thereafter entered into

a confidential settlement agreement whereby Mitsubishi Bank and the Bank of California made payment of $3,864,012 to the taxpayer's attorney and $4,864,547 to the taxpayer.

In his 1995 tax return, the taxpayer reported $1,473,685 as income, most of which was deemed by the taxpayer to be "taxable interest" with the explanation that the compensatory damages, the punitive damages, and the interest on the part of the award used to pay his attorney's fees were excludable from his gross income. The I.R.S. disagreed and issued a notice of deficiency regarding the tax payment.

The notice of deficiency explained that $8,103,559 of the settlement proceeds were reportable as income and not the $1,421,420 that the taxpayer reported, thus increasing his taxable income to $6,682,130. The I.R.S. then recalculated the taxpayer's itemized deductions and determined that the alternative minimum tax applied, which had the affect of reducing or eliminating the expense deduction for the payment that was made to the taxpayer's attorney. The I.R.S. therefore concluded that the taxpayer owed an additional $1,708,216 in income taxes for the 1995 tax year.

The Ninth Circuit Court of Appeals agreed with the Tax Court that the amount attributed to punitive damages should be included in the taxpayer's income since he could not show that such damages were based "on account of personal injury or sickness." Banaitis, 340 F.3d at 1081. The court, however, disagreed with the Tax Court regarding the tax treatment of the taxpayer's attorney's fees. The court reasoned that since Oregon state law vests attorneys with property interests that cannot be extinguished or discharged by the parties to the action except by payment to the attorney, the payments

made to the taxpayer's attorney are not income to the taxpayer. Banaitis, 340 F.3d at 1083. The Smiths point out that the court's decision on attorneys fees is currently before the U.S. Supreme Court on certiorari. (Appellee's Brief at 30).

The court observed the following facts in Footnote 1 of its opinion: Oregon has a split-recovery statute that awards a portion of the punitive damages to the state; on March 7, 1996, the taxpayer wrote to the state and asked it to confirm in writing that it had no interest in the money that the taxpayer had recovered in the case; the state refused to give such a confirmation; and "sometime later" the taxpayer paid the state $150,000.

From this, the Smiths argue that the I.R.S. "has assessed income tax liability based on the AMT upon taxpayers who have recovered punitive damages on the portion paid to the state under state statute." (Appellee's Brief at 29). While perhaps technically true, this argument distorts the ruling in the case. At all times pertinent to that case, the taxpayer claimed ownership of all of the punitive damages that he recovered in the settlement. Subsequently, in 1996 the taxpayer requested Oregon to confirm that it had no interest in the money that he recovered. When the state refused the taxpayer's request based on its split-recovery statute, the taxpayer "some time later" paid Oregon State $150,000. It is not known how that payment was ultimately treated by the I.R.S. and the taxpayer. But for the 1995 tax year, the split-recovery statute was not an issue since the taxpayer claimed that he owned all of the money that he received during that year.

If anything, the decision in Banatis supports the State's argument in the present case. In Banatis, the court ruled that the taxpayer's attorney's fees were not to be

included as income to the taxpayer because the attorney has a proprietary interest in those fees. It is the same here. Because the State has a proprietary interest in a portion of the punitive damage judgment, the amount to be paid to the State is not income to the Smiths.

The Smiths also cite to a news commentary that referred to a last minute amendment to a Senate bill that was introduced by Senator Orrin Hatch but never passed. That amendment apparently sought to clarify that even though punitive damages are now always taxable to the recipient, any punitive damages that must go to the State under split-recovery statutes will not be taxable to the plaintiff. This reference does little more than point out that the Smiths or other plaintiffs approached the gentlemen senator with an amendment that would have clarified a point of law and that, for whatever reason, the amendment never made it out of committee.

What the Smiths essentially argue is that it would be unfair for the court to find the Punitive Damages Awards Act constitutional because of the potential tax treatment that they would receive under the Tax Code. As the State has previously argued, it is the legislative branch that should be asked to address that issue and not the court. (Appellant's Brief at 19).

V. A VIOLATION OF THE SEPARATION OF POWERS WOULD OCCUR IF THIS COURT WERE TO DECLARE THAT THE PUNITIVE DAMAGE AWARDS ACT IS UNCONSTITUTIONAL AND THEREBY TAKE FROM THE LEGISLATURE ITS PREROGATIVE IN LAWMAKING.

The Smiths argue that because the judgment names them, and only them, on the judgment and because the State never intervened in the original case to claim a vested

interest in the judgment, the judgment is beyond rewrite or revision to give the State an interest in a portion of that judgment. Therefore, according to the Smiths the Legislature is attempting through enactment of the split-recovery statute to invade and revise a final judgment of the court in violation of the Separation of Powers article of the Utah Constitution. (Appellee's Brief at 43). Given the nature of punitive damages under Utah law, the Smiths' argument fails.

Under Utah law, a party does not have a cause of action for punitive damages. DeBry v. Cascade Enterprises, 879 P.2d 1353, 1359 (Utah 1994). As a result, a party does not have a constitutionally protected right to any amount of punitive damages until such damages are awarded in a judgment. In addition, the legislature has the authority to modify or abolish the ability of a party to claim punitive damages. Jackson v. Mateus, 2003 UT 18, ¶ 21, 70 P.3d 78, 83 (common law may be modified by statute).

In this case, the legislature restricted the amount of punitive damages that the Smiths could recover before the final judgment awarding such damages was entered. It does not matter that the judgment did not name the State as a judgment creditor since the Smiths could not obtain a right that is greater than that allowed by law. See Spanish Fork Westfield Irr.Co. v. District Court of Salt Lake County, 99 Utah 527, 104 P.2d 353, 359 (1940). It does not matter that the State did not intervene before the judgment was entered to claim a vested interest since the legislature had already determined that a portion of the punitive damages judgment was to be paid to the State. As a result of the enactment of the Punitive Damages Awards Act, the Smiths' right to punitive damages

vested in the first $20,000.00 and then 50% of the balance of the punitive damages after deducting attorneys fees.

This is not a case about protecting the right of the judiciary to not have its final judgments tampered with by the legislature. Rather, this case is about the court taking away from the legislature the prerogative of lawmaking. Indeed, it is only if this Court were to agree with the Smiths and affirm the trial court's construction of the statute that there would be a violation of the Separation of Powers by the judiciary.

VI. THERE IS NO VIOLATION OF EQUAL PROTECTION BECAUSE THE LEGISLATURE HAS A LEGITIMATE PURPOSE IN ENACTING THE STATUTE AND THERE IS A REASONABLE RELATIONSHIP BETWEEN THE LEGISLATIVE OBJECTIVES AND ANY DIFFERENCE IN THE TREATMENT OF PLAINTIFFS LIKE THE SMITHS.

The Smiths argue that the Punitive Damage Awards Act violates the equal protection guarantees of the Utah and U.S. Constitutions because "it discriminates between similarly situated persons by taking 50% of punitive damage awards but leaving untouched statutory punitive damage awards" and because "it discriminates against similarly situated persons by taking 50% of punitive damage awards but not taking punitive damages obtained by settlement." (Appellee's Brief at 45). These arguments are without merit.

This Court has made it clear that if there is no violation of equal protection under the Utah Constitution, then there is no violation of equal protection under the U.S. Constitution. Blue Cross and Blue Shield of Utah v. State, 779 P.2d 634, 637 (Utah 1985). Therefore the analysis of the Smiths' equal protection arguments centers on what

is required under the Utah Constitution. Article I, section 27 of the Utah Constitution states that "All laws of a general nature shall have uniform operation."

In Blue Cross and Blue Shield of Utah, 779 P.2d at 637, this Court stated that the concept behind equal protection is that the legislature should be "restrained from the fundamentally unfair practice of classifying persons in such a manner that those who are similarly situated with respect to the purpose of a law are treated differently by that law, to the detriment of some of those so classified." This Court further explained that when scrutinizing a legislative measure under the equal protection clause, the court must determine "whether the classification is reasonable, whether the objectives of the legislative action are legitimate, and whether there is a reasonable relationship between the classification and the legislative purposes." Id. at 637. In areas of purely economic regulation, the court gives broad deference to the legislature. Id. at 637.

In the present case, all persons who obtain a punitive damage judgment pursuant to the statute are treated the same. The plaintiffs that bring actions pursuant to the unlawful detainer statute, the Utah Antitrust Act, etc. are treated differently than the Smiths regardless of the enactment of the Punitive Damages Awards Act. The availability and set amount of punitive damages under those other statutes are proscribed by the legislature to meet the purposes of those particular enactments.

The purpose of the Punitive Damage Awards Act is to bring about tort reform. (Appellant's Brief at 17). One of the legislative objectives in meeting this purpose is to reduce the cost to the liability industry by taking away the incentive of

plaintiffs to litigate to obtain large punitive damage awards. Another objective is to reduce the windfall that a plaintiff obtains for harm done to the public. These are legitimate objectives of the legislature. The statute accomplishes these objectives in a reasonable fashion by requiring any punitive damage judgment to be divided with the State. Consequently, there is no violation of equal protection.

The same conclusion is reached with those who settle before judgment is entered. Because the statute limits the amount of punitive damages that an injured party can recover, there is an incentive for the injured party to settle. Likewise, because the statute does not place a cap on the amount of punitive damages that can be ordered to be paid, there is an incentive for the tortfeasor to settle. Out-of-court settlements generally result in reduced costs to parties. As a result, any difference is reasonably related to the purposes of the statute and there is no violation of equal protection.

VII. THE STATE IS ENTITLED TO THE INTEREST THAT HAS ACCRUED ON ITS PORTION OF THE PUNITIVE DAMAGE JUDGMENT.

The Smiths argue that even if the Court were to reverse the trial court and uphold the statute, the Court should determine that the interest that has accrued from the date of the judgment through the date of payment is vested in them. They base their argument on their construction of the statute that the State's entitlement starts to run only when the judgment is paid and not entered. (Appellee's Brief at 48). The State's response to this argument follows its other responses to the Smiths' arguments. Since the State's interest was created when the punitive damages were awarded in the judgment, it is entitled to the interest that has accrued on its portion of the punitive damages judgment.

If the Smiths' ability to have a vested right in punitive damages was limited by law as the State argues, then their ability to receive interest would also be limited to the amount of interest that accrued on their vested right.

CONCLUSION

Appellant respectfully requests the Court to reverse the decision of the trial court and rule that the Punitive Damages Award Act, Utah Code Ann. § 78-18-1(3) is constitutional and enforceable against the Smiths.

DATED this 18th day of January, 2005.

MARK L. SHURTLEFF
Attorney General

KEVIN V. OLSEN
Assistant Attorney General
Attorneys for Rule 19 Defendant/Appellant

CERTIFICATE OF SERVICE

I hereby certify that on the 18th day of January, 2005, I served two true and exact copies of the foregoing Reply Brief of Rule 19 Defendant/Appellant, postage prepaid, on the following:

Robert S. Campbell, Jr.
VAN COTT, BAGLEY, CORNWALL
& McCARTHY, P.C.
50 South Main, Suite 1600
Salt Lake City, Utah 84144-0450

James S. Jardine
RAY, QUINNEY & NEBEKER
36 South State Street #1400
Salt Lake City, Utah 84111

Reed L. Martineau
Rex E. Madsen
SNOW, CHRISTENSEN & MARTINEAU
10 Exchange Place, Eleventh Floor
P.O. Box 45000
Salt Lake City, Utah. 84145-5000

Donna Arrigo